RSC Republican Study Committee

Rep. Jeb Hensarling (R-TX), Chairman
Russ Vought, Executive Director
132 Cannon House Office Building
Washington, DC 20515

www.house.gov/hensarling/rsc
ph (202) 226-9717 / fax (202) 226-1633

RSC Policy Brief:
H.R. 5715, Ensuring Continued Access to Student Loans Act of 2008
(Miller, D-CA)

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Last week marked a major turning point in the ongoing debate regarding a pending student loan predicament, as Senate Health, Education, Labor and Pensions Committee Chairman Ted Kennedy (D-MA) and House Education and Labor Committee Chairman Miller (D-CA) each announced that they would be introducing legislation (H.R. 5715, the Ensuring Continued Access to Student Loans Act of 2008 and S. 2815, the Strengthening Student Aid for All Act) seeking to ensure the continued availability of student financial assistance. In light of tomorrow's markup of H.R. 5715 in the Education and Labor Committee, this policy brief outlines initial concerns regarding Chairman Miller's proposal, and the effects that previous legislation has had on the loan market.

Student Loan Programs Background:

The federal government provides subsidized and unsubsidized loans to parents and students for higher education (both undergraduate and graduate) using two major programs: the Federal Family Education Loan (FFEL) program and the Direct Loan (DL) program. The FFEL loan program offers subsidized loans provided to students from private lenders. Conversely, in the DL program, the federal government acts as the lender itself and provides the capital for all loans. In FY 2007, these programs provided $63.9 billion in new loans to students and their parents. In that year, the FFEL program provided 11,359,000 new loans averaging approximately $4,494 each, and the DL program provided 2,791,000 new loans averaging approximately $4,603 each.

For loans subsidized by the federal government, the government pays the interest while the student is enrolled as at least a part-time student. The government does not pay the interest on unsubsidized loans.

Impact of Recent Legislation on the Student Loan Market:

Last September, the President signed H.R. 2669, College Cost Reduction and Access Act (CCRA), into law. H.R. 2669 is having serious effects in the market. The CCRA passed as financial markets were undergoing a "credit crunch" that raised the cost of borrowing for financial institutions. Among the effects of H.R. 2669, the burden of private lenders participating in the FFEL program has increased drastically. By reducing subsidies to lenders at a time when interest rates on the market were rising, the CCRA has made lenders participation in the program less attractive, causing some to pull out of the program and creating access difficulties for students and institutions.

Many of the offsets in H.R. 2669—which were included to pay for large increases in mandatory spending—have increased the costs for lenders to provide loans through the program. As such, the legislation discouraged lenders from participating in the FFEL program.

Direct Loan Program vs. Federal Family Education Loan Program:

Some conservatives may be concerned that Chairman Miller's proposal is part of a larger effort by some Democratic lawmakers to breathe new life into the Direct Loan (DL) program, and at the same time, stifle the Federal Family Education Loan (FFEL) program. Similar proposals have been made in the past, including Senator Kennedy's effort during the 109th Congress, S. 754, the Student Aid Reward Act of 2005, which sought to encourage universities to use the DL program, instead of participating in the FFEL program.

The FFEL program has been extremely successful in efficiently providing students with access to college loans. According to a report by America's Student Loan Providers, as of 2004, 83% of schools exclusively used the FFEL program to provide financial assistance to students. At that same time, only 11% of schools used only the DL program, while the remaining 6% utilized both. In addition, another report by American's Student Loan Providers shows that FFEL loans cost taxpayers significantly less than DL.

Summary of Chairman Miller's draft bill:

The bill would increase unsubsidized Stafford loan limits for undergraduate and graduate students by $2,000. Furthermore, Chairman Miller's proposal would provide a grace period deferment for parents of PLUS loans (loans given to parents only; PLUS Loans are available through both the FFEL and the DL programs).

The bill would also clarify that existing law gives the Secretary of Education the authority to advance federal funds to guaranty agencies in the event that they do not have sufficient capital to originate new loans. The Secretary believes that this authority already exists. According to statements made by the Republican Education and Labor Committee staff,

> The Secretary has determined that she has the authority to issue mandatory advances of funds to guaranty agencies. The Secretary also announced that she plans to meet with the guaranty agencies to discuss the plans for implementation of the lender of last resort program.

Chairman Miller's proposal also gives the Secretary of Education the temporary authority to purchase loans from lenders in the federal guaranteed loan program (FFEL) and transfer these to Direct Loans. Some conservatives may be concerned that this provision would have the effect of transferring major portions of the FFEL program to be serviced directly by the Department, representing a significant expansion of the federal government's scope and role in the student loan marketplace. Some conservatives may also be concerned that the Department may not be technically equipped to handle such a rapid increase in direct student lending, potentially resulting in requests for supplemental appropriations by the Department and creating confusion for borrowers whose loan servicing has suddenly been transferred into federal hands.

The bill also includes Sense of Congress language that states that during this time when the economy is fragile and higher education and retraining opportunities are more important than ever, that federal financial institutions, such as the Federal Financing Bank and the Federal Reserve, should consider using available authorities to assist in ensuring that students and families can access federal student loans.

By way of further information, Senator Kennedy's proposal, S. 2815, includes many of the same provisions as Chairman Miller's proposal, with an additional provision which seeks to increase mandatory Pell grant amounts. Increasing mandatory Pell grant amounts could encourage higher appropriation levels in order to sustain the same maximum Pell grant amount (thus increasing federal spending). At this time, Chairman Miller's proposal does not include this provision.

Conclusion:

Many conservatives remain concerned that the CCRA cut lender subsidies by $21 billion at a time when financial and credit markets were in significant turmoil, rather than adapting the legislation to reflect new conditions in the capital markets that were developing at the time of the bill's passage last fall. As an example, Texas-based Brazos Higher Education Service Corp. has become the latest student lender to stop making new loans to students through the Federal Family Education Loans (FFEL) program for the upcoming 2008-2009 academic year. According to FinAid.org, Brazos is just another private lender—topping a list of 26 others—which has stopped originating federal loans.

Some conservatives may be concerned that the Democrats' response to their ill-timed enactment of CCRA furthers government intervention and spending, by increasing federal loan limits and providing greater incentives for participation in DL programs.

According to a National Review article published after the CCRA passed, the effects of the CCRA were foreseen:

> Loan providers will certainly feel the pain of a $20 billion subsidy cut. If lots of lenders do leave the field, which they may, future student borrowers will also feel the pain. Unfortunately, CCRA doesn't justify those risks.
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> The excessive interest cuts and stingy grant-award raises [in CCRA] add up to, essentially, an expensive handout for the middle class. And it continues Congress's trend in reforming higher education aid: more for middle-class voters, and not nearly enough for the poor students for whom federal aid was designed.
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> On top of all this, CCRA doesn't put the screws on colleges to keep their tuition hikes in check, either. Economics 101 tells us that if colleges and universities can continue to count on the U.S. government to increase federal aid, tuition at those schools will also increase. That happens for several reasons, not least of which is

> that federal dollars will, in effect, subsidize tuition hikes, making them less costly to consumers than they actually would be. Middle-class students have more financial wiggle room — plus, they often receive generous merit-based aid packages from colleges desperate to attract talented youngsters. Poor kids lose out …

Finally, since the Department of Education already considers that it has existing authority to advance federal funds to guaranty agencies in the event that they do not have sufficient capital to originate new loans, conservatives may be concerned that the only effects of Chairman Miller's proposal would be to increase the federal government's involvement in the student loan market, and create a bias toward more costly DL programs.

RSC Staff Contact: Sarah Makin, sarah.makin@mail.house.gov, (202) 226-0718;
Chris Jacobs, Christopher.Jacobs@mail.house.gov, (202) 226-8585.

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